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Communications

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

August 7, 1998

Ms. Michelle Carey
Common Carrier Bureau
Federal Communications Commission
1919 M Street, N.W.
Room 544
Washington, D.C. 20554

ORIGINAL

Re: Ex Parte Presentation

Joint Applications of WorldCom, Inc. and MCI Communications Corporation
CC Docket No. 97-211

Dear Ms. Carey:

When I met with you and other Commission staff on July 6, 1998, you asked that Level 3 Communications, Inc. ("Level 3") respond to a number of questions regarding WorldCom/MCI's refusal to enter into peering arrangements with new facilities-based national networks such as Level 3. Attached please find Level 3's responses to these questions.

As set forth herein, Level 3 continues to believe that, notwithstanding MCI's divestiture of its Internet business to Cable & Wireless, the Commission should condition its approval of the WorldCom/MCI license transfer applications upon an agreement by the merged company to enter into peering arrangements with any company that meets either WorldCom's or MCI's existing peering guidelines, absent traffic and balance requirements. Such a condition would ensure that the merger will not disadvantage facilities-based backbone providers like Level 3, but without permitting "free riders" on the WorldCom/MCI network or involving the Commission in ongoing regulatory role.

Pursuant to Section 1.1206(b) of the Commission's rules, two copies of this presentation are being filed with the Secretary, FCC.

Should there be any questions concerning this matter, please contact the undersigned.

Very truly yours,

Terrence J. Ferguson
Senior Vice President and General Counsel

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Enclosures

cc (w/encl.): Chairman William E. Kennard
Commissioner Susan Ness
Commissioner Harold Furchtgott-Roth
Commissioner Michael Powell
Commissioner Gloria Tristani
John T. Nakahata, Office of the Chairman
Thomas C. Power, Office of the Chairman
James Casserly, Office of Commissioner Ness
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Catherine R. Sloan, WorldCom, Inc.

LEVEL 3 RESPONSES TO FCC QUESTIONS

1. DOES DIVESTITURE OF MCI'S INTERNET BUSINESS ELIMINATE THE NEED FOR ADDITIONAL CONDITIONS ON WORLDCOM/MCI'S INTERNET BUSINESS?

No. MCI's divestiture of its Internet business to Cable & Wireless plc ("C&W") does not remove the profound anticompetitive consequences that the WorldCom/MCI merger could have on the emergence of competition from facilities-based providers of IP-based services like Level 3. To the contrary, the combination of the largest Internet backbone provider and the second-largest long distance company significantly increases the merged entity's incentives to impede or refuse to grant such providers interconnection with its Internet backbone in order to preserve the substantial Internet backbone business it will retain after the divestiture and to protect its substantial circuit-switched telephone business.

Legacy Network. For WorldCom, the merger would fundamentally alter the relative importance of the Internet and the telephone business, giving it a substantial incentive to use its continuing control of its Internet backbone to preclude interconnection by IP-based competitors that potentially threaten its legacy telephone business. Revenues from WorldCom/MCI's legacy networks would account for approximately 70 percent of the total revenues of the merged entity.

Internet Competition. The merger also provides WorldCom/MCI with the opportunity to engage in anticompetitive tactics to advantage its still substantial Internet business. While MCI argues that the divestiture fully addresses all competitive concerns implicated by the merger of MCI and WorldCom, WorldCom/MCI will likely retain critical portions of the infrastructure necessary for an Internet business, including valuable dedicated software and operations support systems.¹⁷ Additionally, to the extent that WorldCom and MCI both provide Internet services to the same customer, the divestiture provides that a combined WorldCom/MCI will likely compete for, and retain, that customer's Internet business. Even without such provisions, however, the divestiture described by MCI will have little long-term importance to the Internet business of WorldCom/MCI. Level 3 estimates that WorldCom/MCI will replace the divested Internet revenues in less than three months.

¹⁷ See MCI Reply Comments at 5 (filed July 15, 1998).

2. IN LIGHT OF THE FACT THAT LEVEL 3 CANNOT OBTAIN PEERING ARRANGEMENTS WITH ANY TIER 1 PROVIDER, WHY ARE LEVEL 3'S PEERING CONCERNS RELEVANT TO THE WORLDCOM/MCI LICENSE TRANSFER APPLICATIONS?

WorldCom is the leading provider of Internet backbone services. By adding MCI's network to an infrastructure that already includes UUNET, CNS, and ANS,^{2/} the merger will enhance and enlarge WorldCom's position in the Internet backbone market. Experience has shown that WorldCom has modified its peering requirements in order to preserve its accumulated share of the Internet backbone market

WorldCom/MCI's traffic volume and balance requirements will serve only to impede interconnection with nascent facilities-based competitors – much as AT&T sought to forestall competition from MCI by denying it equal access to the Bell System local telephone exchanges prior to the AT&T divestiture. AT&T's opposition to interconnection delayed the consumer benefits of long distance competition. WorldCom/MCI's refusal to interconnect with other Internet backbones on terms comparable to those provided by WorldCom/MCI to itself internally or to third parties on comparable interconnection links will likewise harm consumers by delaying the economic benefits of a shift from circuit-switched networks to packet-switched networks. The Level 3 network is based on packet-switched technology that makes more efficient use of network capacity than conventional circuit switching, enabling it to move information at a much lower cost.

Because WorldCom is currently the market leader in the Internet backbone market, other "Tier 1" backbone providers have followed WorldCom's practice of imposing traffic and balance requirements as a means to refuse to peer with new, nationally-based providers like Level 3. Just as Tier 1 providers have all modified their agreements to conform with WorldCom's modified peering practices, however, these providers will likely change their existing agreements if the FCC imposed a peering condition on the WorldCom/MCI license transfer application.^{3/}

^{2/} WorldCom owns a majority of another major backbone, GridNet, and has an interest in a fifth, Verio.

^{3/} Significantly, Sprint, a Tier 1 provider, recently confirmed WorldCom's dominant position in the Internet backbone market and its influence on peering. In comments in this docket, Sprint stated, "[I]f, after the merger, the combined WorldCom/MCI entity refuses to enter into settlement-free peering arrangements with competing core backbone providers, including those that are already in the market, it will be especially difficult for these competitors to obtain satisfactory alternative settlements-free routing arrangements from the remaining core providers." Sprint Comments, CC Docket No. 97-211 (Mar. 13, 1998).

**3. AREN'T TRAFFIC VOLUME AND BALANCE REQUIREMENTS
LEGITIMATE MEANS OF MINIMIZING "FREE RIDER" CONCERNS?**

MCI's and WorldCom's peering principles contain numerous requirements designed to deter free riders, including connectivity, infrastructure, routing, and support service requirements. Taken together, these provisions guarantee that WorldCom will continue to peer only with companies that have the means to route traffic on a bilateral and equitable basis and the ability to provide WorldCom with similar services to those provided by WorldCom. By providing peering agreements only to similarly-sized, facilities-based national backbone networks that are capable of delivering capacity at sufficient speeds to a sufficient number of geographic locations, WorldCom can effectively minimize free riders -- without also requiring minimum traffic volumes and balance. As noted above, volume and balance requirements serve only to deter interconnection with facilities-based competitors.

Level 3 is a national network provider which anticipates making an \$8 to \$10 billion investment to construct an international, end-to-end facilities-based network optimized for IP technology. Over the next four to six years, Level 3 estimates that its network will encompass backbone facilities in approximately 50 North American markets and will include a 15,000 mile intercity network. Internationally, Level 3 intends to establish intracity facilities in 17 additional markets in Europe and Asia while deploying a 2,000 mile intercity network across Europe. In light of Level 3's substantial commitment to IP facilities, Level 3 would in no way be a free rider on the WorldCom/MCI network.

In fact, the imposition of traffic volume and balance requirements does not address free riding concerns. In May 1997, when WorldCom's UUNET first announced modifications to its peering standards, UUNET argued that it had invested "hundreds of millions of dollars to create its infrastructure" and should not be required to provide free routing to companies which are too small to reciprocate.^{4/} Level 3 agrees with WorldCom's basic proposition that network infrastructure is expensive. Accordingly, it is no longer appropriate to allow companies that have not invested in the connectivity, infrastructure, and routing capabilities to peer with other, more advanced networks for free. Traffic and balance requirements, however, have nothing to do with these concerns. In light of the fact that IP traffic is growing at an almost exponential rate, the imposition of volume and balance requirements is particularly inappropriate because it will delay the development of new facilities-based networks which are needed to accommodate such demand.

The Commission can remove the most significant threat to competition posed by the pending merger by conditioning approval of the transaction on a commitment by the merged entity to peer with Level 3 and other facilities-based Internet backbone providers that meet the

^{4/} See "Internet Services: UUNET 'Peering' Policy Could be Boon for Equipment Vendors," Telecommunications Reports (May 19, 1997); "UUNET Changes Peering Policy," Telecommunications Alert (May 14, 1997).

companies' existing peering requirements, absent traffic or balance requirements. It is completely appropriate to impose such a requirement as a condition of the instant transaction. Indeed, the first equal access requirements were imposed on the Bell operating companies as part of the decree settling the AT&T antitrust case.^{5/}

4. ARE TRANSIT AGREEMENTS A LEGITIMATE PROXY FOR PEERING AGREEMENTS?

Providing Level 3 with full interconnection rights pursuant to a peering agreement is considerably different from transporting and routing IP traffic pursuant to a transit agreement. Compelling parties to sign transit agreements offers WorldCom/MCI an incentive to abuse its market power when dealing with new entrants and smaller existing backbone providers. First, since transit charges are not disclosed, there is no way of determining whether such charges are unreasonably discriminatory. This uncertainty provides WorldCom/MCI with an irresistible opportunity to place new entrants such as Level 3 at a cost disadvantage in the marketplace.

Second, under a transit agreement, Level 3 would be a customer of WorldCom/MCI rather than a network provider. As a WorldCom/MCI customer, Level 3 would be dependent upon WorldCom/MCI for the delivery of IP traffic. This places Level 3 at a marketing disadvantage because potential customers may be disinclined to take service from a backbone provider who is itself a customer, and not a peer, of another backbone provider.

Third, transit agreements provide for the transmission of traffic over the entire routing table. Level 3 has peering arrangements with 12 other Internet backbone providers, and does not need a transit agreement with WorldCom/MCI to deliver its traffic to these other networks. If Level 3 is forced to enter into a transit agreement with WorldCom/MCI in order to exchange traffic with the merged entity, the costs to Level 3 in the form of charges for unnecessary transmission services could be substantial. As a customer rather than a peer, moreover, Level 3 would be unable to provide its customers with all of the advantages of its state-of-the-art national network.

^{5/} United States v. AT&T, 552 F. Supp. at 195-200 (D.D.C. 1982), *aff'd sub nom. Maryland v. United States*, 460 U.S. 1001 (1983). See also United States v. GTE Corp., 603 F. Supp. 730 (D.D.C. 1984). The FCC did not extend equal access obligations to the non-Bell local exchange carriers until 1985. MTS and WATS Market Structure Phase III, 100 F.C.C. 2d 860, 57 R.R.2d 1303 (1985).

**5. ASSUMING ARGUENDO THAT THE FCC SHOULD CONDITION THE
LICENSE TRANSFER APPLICATION UPON A MODIFICATION OF
WORLDCOM/MCI'S PEERING ARRANGEMENTS, WHAT WOULD THE
COMMISSION'S ORDERING CLAUSE LOOK LIKE?**

Level 3 believes that the Commission can easily condition approval of the WorldCom/MCI license transfer application upon a modification of WorldCom/MCI's peering arrangements, without establishing an extensive regulatory regime. Such a condition could take the form of the following ordering clause:

It is FURTHER ORDERED that WorldCom and MCI shall provide peering arrangements to all facilities-based providers of Internet transmission services that meet the parties' pre-existing peering guidelines, but without the traffic volume or balance requirements that are to be included as part of such guidelines.

Compliance with such a condition could be based on record-keeping and dispute resolution procedures currently employed by parties with existing peering arrangements. Quality of service can be measured simply and objectively by each interconnecting party using established network statistics collection tools. Using these procedures, service quality can be measured from connections between a point on the Level 3 network to a point on the WorldCom/MCI network and the quality of WorldCom/MCI-only connections with Level 3 can be compared to other WorldCom connections over a period of time. Evidence of quality degradation could be presented to WorldCom in the first instance and then, if necessary, to the Commission.